

May 27, 2010 – China: The Canary in the Coal Mine?

During secular bear markets (defined here: <http://davefulkerson.com/images/August08.pdf>) history shows us “buy and hold” simply doesn’t work. Successful investing during turbulent times requires insight into what some of the “canaries in the coal mine” are to help us identify when the stock market advance may be coming to an end.

At the end of the bull market advance in 2007, the Advance-Decline line warned us of the coming correction. See the November, 2007 newsletter warning of the A-D line divergence here: <http://davefulkerson.com/images/November07.pdf>.

Another indicator that helped us see the trend changes in the stock market over the last three years has been the action of the Shanghai stock market. The chart below shows the S&P500 index in green and the Shanghai index in red. A major decline began in the Shanghai market in January of 2008, marked by point 1 on the chart. The major crash in our market did not begin for another nine months at point 2.



From here, Shanghai bottomed in early November, 2008 at point 3. The S&P500 index bottomed five months later at point 4 after the Shanghai index was already beginning to rise, signaling our bear market may be coming to an end. In August, '09, Shanghai put in a top at point 5 and has been making lower highs since. This is bearish. The S&P500 continued to rally for another eight months and registered the high of the rally at point 6 in April.

To help confirm if our market has topped and we are in for another bear market, watch to see if the Shanghai index breaks through major support (marked by S1) and heads south. If S1 is taken out in the coming days or weeks, it would be a good indication the U.S. bull market we have been in since March of 2009 has come to an end. And don't forget to watch the A-D line!

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